



SACHI A. HAMAI
Interim Chief Executive Officer

County of Los Angeles CHIEF EXECUTIVE OFFICE

Kenneth Hahn Hall of Administration
500 West Temple Street, Room 713, Los Angeles, California 90012
(213) 974-1101
<http://ceo.lacounty.gov>

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July 21, 2015

To: Mayor Michael D. Antonovich
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From: Sachi A. Hamai
Interim Chief Executive Officer

STATUS REPORT – AUDIT OF WORKERS' COMPENSATION THIRD-PARTY ADMINISTRATION SERVICES

On October 22, 2013, the Board approved a recommendation to find that workers' compensation claims third-party administration (TPA) services can be performed more economically by independent contractors. At that time, the Board instructed the Chief Executive Officer (CEO) to incorporate audit criteria which includes any known criminal activity, negligence, and overall contract compliance when evaluating TPA performance. This is the third bi-annual report on existing TPA performance.

Background

The County of Los Angeles (County) Workers' Compensation Program (Program) was established under the authority of County Code Section 5.31.050. A Program mandate is to ensure the full provision of benefits under the law to employees whose injuries arise out of, and in the course of, employment. The Program is the largest local agency workers' compensation program in the State of California, which issues approximately 500,000 payment request transactions annually. The Program is bound by a complex set of statutory, regulatory, and case law requirements that complicate claims administration and present inherent system risks.

A variety of quality control mechanisms are implemented to evaluate TPA performance, protect the County from improper payments initiated by TPA staff, and ensure adequate separation of duties. Payment transaction system functions are separated to require at least two individuals to release a payment transaction. Approval levels require at least two authorized individuals to release a workers' compensation payment transaction.

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Background (Continued)

Generally, the following authorization requirements apply to workers' compensation benefit payment transactions:

- Payments up to \$4,000 require one authorization and a separate individual to release the transaction;
- Payments exceeding \$4,000 require two authorizations and a separate individual to release the transaction;
- Payments exceeding \$5,000 require three authorizations and a separate individual to release the transaction;
- Payments exceeding \$7,500 require four authorizations and a separate individual to release the transaction; and
- Payments exceeding \$75,000 require five authorizations and a separate individual to release the transaction.

On-Site County Representatives

Currently, six On-Site County Representatives (OSCRs) are headquartered at TPA facilities. These County employees perform various functions. Their payment transaction audit and review functions include the following:

- Reviewing and authorizing payment transaction requests exceeding \$7,500;
- Evaluating and authorizing payment transaction requests initiated by a Workers' Compensation Appeals Board (WCAB) order or award;
- Performing fiscal reconciliation of all claims resolved by WCAB indemnity order, WCAB indemnity award, or indemnity payment requests exceeding \$7,500;
- Identifying and recovering costs associated with penalties, excess costs, or overpayments caused by the contractor's actions or failures to act as defined in the contract; and
- Identifying and investigating payment transactions that are potentially fraudulent and notifying CEO Risk Management Branch when such are identified.

On-Site County Representatives (Continued)

Additional OSCRs' responsibilities include:

- Providing subject matter expertise to County departments and injured workers to expedite the equitable resolution of workers' compensation benefit issues and control costs consistent with the provision of workers' compensation benefits allowable under the law;
- Attending regularly scheduled department claim reviews to minimize County departments' exposure to workers' compensation and disability management liabilities;
- Assisting County Counsel and contract law firms obtain information needed to properly defend litigated workers' compensation claims; and
- Analyzing and approving workers' compensation settlements or stipulations consistent with the negotiation levels established in the workers' compensation TPA contracts.

Since January 1, 2015, OSCRs reviewed approximately 450 payment request transactions exceeding \$7,500 per month. Additionally, the OSCRs reviewed approximately 850 payment transactions generated by a WCAB order or award per month. Over 60 percent of those transactions required a claim file fiscal reconciliation.

Fiscal Reconciliation Process

The fiscal reconciliation process, or claim file balancing, requires the OSCRs to evaluate the workers' compensation award or order and ensure the past, present, and future benefit stream comports to the Court award or order. This process requires a careful review of indemnity benefits owed and paid, benefits currently being paid, and payments that will be issued in the future ("cycled" or system-generated payments). The reconciliation process includes calculating savings caused by an ordered commutation of benefits. Workers' compensation claim files that do not balance are returned to the TPA for correction or reimbursement.

Since the fiscal reconciliation process evaluates the indemnity benefit stream, it allows OSCRs to review many payments without approving all the individual payments issued on a particular workers' compensation claim. An analysis of fully developed claims (FY1994-95) demonstrated that 90 percent of all indemnity payment transactions and 89 percent of all indemnity paid amounts issued on workers' compensation claims had a Court award or order. Therefore, the fiscal reconciliation process allows a relatively small number of County employees to assess a large number of workers' compensation indemnity payments, ensuring the accuracy of such payments.

Random Transaction Audit

The purpose of the random transaction audit is to select and review individual payment transactions that may be split (to circumvent payment authority levels) or represent duplicate payments (payments issued to the same payee with overlapping service dates) to ensure payment process controls are being systematically applied, ensure the individual payment is appropriate (not split or a duplicate payment caused by the inappropriate application of a "T" override), and identify potential fraud or abuse executed by TPA staff.

Methodology

During this reporting period, CEO Risk Management Branch staff randomly selected 200 payment transactions from a sample of 3,150 transactions that required a "T" override. The "T" override is manually applied to payment transactions that the workers' compensation claims management system will not release because of potential duplication. Once the "T" override is applied, the payment transaction is released. Such payment transactions represent the population most likely to be the result of inappropriately splitting a payment or creating a duplicate payment. Each payment transaction is audited to evaluate compliance with established protocols, unintended excess cost to the County, or TPA fraud. During the audit, CEO Risk Management Branch staff reviewed payment transactions to determine the following:

- The payment transaction was appropriate and did not result in a duplicate payment;
- The payment transaction was appropriate and did not result in the splitting of the payment to circumvent authority levels;
- The amount of the duplicate payment and potential excess cost to the County;
- The payment transaction required a "T" override;
- The payment is approved in compliance with established authority levels;
- That payment transaction supporting documentation demonstrates appropriate segregation of duties; and
- Whether the payment transaction was issued as a result of potential fraud.

Findings

The audit findings are summarized below:

Transactions Audited	200
Total Paid	\$234,530.07
Split Payments Identified	0
Duplicate Transactions Identified	4
Amount of Duplicate Payments	\$803.63
Transactions Not Requiring "T" Release	17
Transactions Potentially Lacking Appropriate Authority Level	0
Transactions Potentially Lacking Appropriate Segregation of Duties	0
Transactions Identifying Potential Fraud	0

The two largest duplicate payments were for \$317.48 and \$260.90, which were payments issued to two photocopy service companies. These duplicate payments were caused by the same invoices being processed twice. Though the system identified the duplicate, TPA staff applied a manual release causing the duplicate payments. The TPA has been notified and will either recover the overpayment from the photocopy companies or reimburse the County. The second largest duplicate payment, in the amount of \$156.50, was issued to a physical therapy facility. That payment was caused because the same medical charges were processed twice. Though the system identified the potential duplicate, TPA staff applied a manual release causing a duplicate payment. The TPA has been notified and will either recover the overpayment from the medical provider or reimburse the County. The final duplicate payment was for \$68.75 and issued to the pharmacy benefit management company twice for the same dispensed medications. The TPA has been notified and will either offset future medical mileage reimbursement payments to the injured worker or reimburse the County.

SUMMARY

Though the audit did not identify any fraud or abuse, it did find that TPA staff are applying "T" overrides on transactions that do not require them. CEO Risk Management Branch staff found 8.5 percent of the payment transactions audited did not require "T" overrides. This practice, done to expedite benefit delivery, weakens internal controls and may result in duplicate payments and unwarranted costs. TPA management has been notified of these findings and will provide additional training to staff.

The CEO is committed to reducing Program fraud exposure through the continuous improvement of processes. A multi-disciplined approach that includes TPA management and the evaluation of new technologies is required. CEO staff will be meeting quarterly with TPA management to identify improvements in business process monitoring with due consideration given to benefit delivery needs.

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The CEO will provide another audit report to the Board in January 2016.

If you have any questions or would like additional information, your staff may contact Steven T. Robles, Assistant Chief Executive Officer/County Risk Manager, at (213) 351-5346.

SAH:JJ
STR:AR:rn

c: Executive Office, Board of Supervisors
County Counsel